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Finance Bill 2016 PRSA & Personal Pension

PENSION ADVISORY SERVICES

The Finance Bill 2016 has included an amendment to the treatment of PRSAs and Personal Pensions, technically known as Retirement Annuity Contracts (RACs), when clients reach age 75.

What are the proposed changes?

When a PRSA or Personal Pension (RAC) client reaches age 75 their plan will automatically become a vested PRSA or vested RAC respectively, even if they have not yet taken their retirement lump sum.

For PRSA and Personal Pension (RAC) clients who have already reached age 75, their plan will automatically become vested on the passing of the Finance Act.

When a plan becomes a vested PRSA or vested RAC, the client will have 30 days to complete a BCE certificate. The Irish Life PRSA & Personal Pension retirement claim form includes a BCE certificate as part of the form. If clients do not do this then tax at 40% will be deducted from their pension fund as if they have exceeded the €2m Standard Fund Threshold. (An example at the end of this update shows the taxation treatment of an excess over SFT.)

In addition, the Revenue Commissioners will take a stricter interpretation of PRSA and Personal Pension (RAC) legislation going forward whereby clients will have no access to a vested PRSA or vested RAC once they have attained age 75. The only amounts paid out from a vested PRSA would be imputed distribution tax to Revenue annually (but no payments to the client). No distributions will be allowed from a vested RAC. A payment to the client's estate will be permitted on death.

The proposal is that clients will have until 31 March 2017 to take their retirement benefits. After that there will be no opportunity to make any further withdrawals from their vested PRSA or vested RAC, and no option to transfer funds to an ARF or to purchase an annuity after reaching age 75.

This is a change from previous discussions we have had with the Revenue Commissioners when they said that they expected clients to continue to access their vested PRSA benefits after age 75.

When does this new legislation apply?

This will apply from the passing of the Finance Act which is expected mid to late December 2016.

What is Irish Life's view on this change?

We do not believe that it is appropriate for clients not to be able to access their pensions over age 75. We have contacted Revenue and Department of Finance (through Insurance Ireland) and Pensions Authority to raise our concerns. Irish Life is concerned by any potential interpretation of Finance Bill 2016 whereby a potentially vulnerable group of clients over age 75 have access to their pensions savings restricted.

What do PRSA and Personal Pension clients approaching age 75 or over age 75 need to do?

There is no change for clients under age 75. The changes introduced only impact clients when they reach age 75.

However, clients with a PRSA or vested-PRSA or Personal Pension will need to consider their options as they approach age 75. In order to be able to access their pension fund beyond age 75 they will need to consider transferring to an ARF / AMRF or purchasing an annuity before age 75. Those already age 75 or over have until 31 March 2017 to do this.

It continues to be the case that the tax free lump sum option is only available when benefits are first accessed.

Clients first need to decide which of the options they wish to avail of. They could transfer their value to an ARF or take a taxable lump sum (subject to the AMRF / guaranteed pension income rules), or use it to purchase an annuity, or a mix of options. They will then need to complete a PRSA & Personal Pension retirement claim form, and an ARF or Annuity application form as appropriate. As part of their claim they will need to inform us of any other pension benefits they have taken retirement benefits from, or transferred overseas, since 7 December 2005, as this is the BCE cert part of the claim form.

Imputed Distribution for vested PRSAs (not applicable to vested RACs)

Irish Life's current process is that we pay actual distributions to clients subject to the imputed distribution. An actual withdrawal is no longer permitted after 31 March 2017 for vested PRSAs from age 75 and over.

This means that income tax and USC will be due each year as if the client had made a withdrawal equal to 5% of the value of the vested-PRSA as at 30 November (6% if total value of all vested-PRSAs and ARFs is over €2,000,000). However, no actual payment will be made to the client.

Death Benefits

Death Benefit options before the passing of the Finance Act

Currently if a client aged 75 or over has an 'unvested' PRSA or Personal Pension then on death the full value of their plan would pass to their estate on death. Inheritance Tax would then apply with the normal thresholds applying. The normal exemption between spouses would apply.

If the client is aged 75 or over has a vested PRSA the on death the vested PRSA is treated in the same way as an ARF on death.

Death Benefit options after the passing of the Finance Act

From the passing of the Finance Act there will be no 'unvested' PRSAs or Personal Pension where a client is aged 75 or over. Such clients aged 75 or over will have a vested PRSA or vested RAC and on death the plan is treated in the same way as an ARF on death.

What is the background to this change?

The background to this change is that some people with funds in excess of the €2m standard fund threshold (SFT) or personal fund threshold (PFT) were using PRSAs and Personal Pensions as a shelter to avoid the excess tax that is intended to apply on retirement to fund values over these thresholds.

Impact on clients now aged 75 or over (up to 31 March 2017)

	PRSA	Vested PRSA	Personal Pension (RAC)
What happens on the passing of the Finance Act?	PRSA will become a vested PRSA	Plan remains a vested PRSA	Personal Pension (RAC) will become a vested RAC
Does the client have to return a BCE certificate to Irish Life?	Yes, the client has 30 days from when the Finance Act is passed to complete a BCE cert. This is part of the PRSA retirement claim form.	No, a BCE cert will have been completed as part of the PRSA retirement claim when the client took their tax free lump sum.	Yes, the client has 30 days from when the Finance Act is passed to complete a BCE cert. This is part of the Personal Pension retirement claim form.
What happens if the client does not return a BCE certificate?	40% of their fund value will be deducted as income tax.	Not applicable as client will have previously returned a BCE cert.	40% of their fund value will be deducted as income tax.
Can the client take a tax free lump?	Yes, up to 31 March 2017.	No, client will have previously taken their tax free lump sum.	Yes, up to 31 March 2017.
Can the client take a taxable withdrawal from the plan?	Yes, the balance of the fund could be withdrawn, up to 31 March 2017. This would be taxable at the client's marginal rate of income tax plus USC.	The fund could be withdrawn, up to 31 March 2017. This would be taxable at the client's marginal rate of income tax plus USC.	Yes, the balance of the fund could be withdrawn, up to 31 March 2017. This would be taxable at the client's marginal rate of income tax plus USC.
What other retirement benefit and transfer options are available?	The balance of the fund can be used to • Purchase an annuity and/or • Invest in an ARF up to 31 March 2017.	The fund can be used to • Purchase an annuity and/or • Invest in an ARF up to 31 March 2017.	The balance of the fund can be used to • Purchase an annuity and/or • Invest in an ARF up to 31 March 2017.
Can the value be left in the plan beyond 31 March 2017	Yes, but no access will be permitted other than on death.	Yes, but no access will be permitted other than on death.	Yes, but no access will be permitted other than on death.
Will an imputed distribution tax apply each year	Yes from 2017. No actual payment will be made to the client.	Yes from 2017. No actual payment will be made to the client.	No.
What is the treatment on death?	ARF rules apply on death	ARF rules apply on death	ARF rules apply on death

Impact on clients who reach age 75 (after 31 March 2017)

	PRSA	Vested PRSA	Personal Pension (RAC)
What happens on the client's 75th birthday?	PRSA will become a vested PRSA	Plan remains a vested PRSA	Personal Pension (RAC) will become a vested RAC
Does the client have to return a BCE certificate to Irish Life?	Yes, the client has 30 days to complete a BCE cert. This is part of the PRSA retirement claim form.	No, a BCE cert will have been completed as part of the PRSA retirement claim when the client took their tax free lump sum.	Yes, the client has 30 days to complete a BCE cert. This is part of the Personal Pension retirement claim form.
What happens if the client does not return a BCE certificate?	40% of their fund value will be deducted as income tax.	Not applicable as BCE cert will have been previously completed.	40% of their fund value will be deducted as income tax.
Can the client take a tax free lump?	A tax free lump sum is available prior to their 75th birthday.	No, client will have previously taken the tax free lump sum.	A tax free lump sum is available prior to their 75th birthday.
Can the client take a withdrawal from the plan?	Prior to their 75th birthday the balance of the fund could be withdrawn subject to the client having invested €63,500 in an AMRF or annuity purchase, or being in receipt of pension income of €12,700. The withdrawal is taxable at the client's marginal rate of income tax plus USC (plus PRSI to age 66).	Prior to their 75th birthday the fund could be withdrawn subject to the client having invested €63,500 in an AMRF or annuity purchase, or being in receipt of pension income of €12,700. The withdrawal is taxable at the client's marginal rate of income tax plus USC (plus PRSI to age 66).	Prior to their 75th birthday the balance of the fund could be withdrawn subject to the client having invested €63,500 in an AMRF or annuity purchase, or being in receipt of pension income of €12,700. The withdrawal is taxable at the client's marginal rate of income tax plus USC (plus PRSI to age 66).
What other retirement benefit options are available?	Prior to their 75th birthday the balance of the fund can be used to • Purchase an annuity and/or • ARF / AMRF	Prior to their 75th birthday the fund can be used to • Purchase an annuity and/or • ARF / AMRF	Prior to their 75th birthday the balance of the fund can be used to • Purchase an annuity and/or • ARF / AMRF
Can the value be left in the plan beyond their 75th birthday	Yes, but no access will be permitted other than on death.	Yes, but no access will be permitted other than on death.	Yes, but no access will be permitted other than on death.
Will an imputed distribution tax apply each year	Yes. No actual payment will be made to the client.	Yes. No actual payment will be made to the client.	No.
What is the treatment on death?	ARF rules apply on death	ARF rules apply on death	ARF rules apply on death

APPENDIX 1 – TAX INFORMTION

What tax applies on drawdown of retirement benefits from a vested-PRSA

Withdrawals from a vested-PRSA, AMRF / ARF or Annuity income, are subject to PAYE. Further information on the tax treatment of retirement options are set out below.

In addition for clients whose total pension benefits have exceeded the €2,000,000 Standard Fund Threshold (SFT) or Personal Fund Threshold (PFT), the excess over the SFT / PFT will be subject to tax at the higher rate of income tax (currently 40%). Since 7 December 2005 every time an individual becomes entitled to receive a pension benefit, e.g. retirement lump sum, annuity, ARF, vested PRSA etc. or they transfer a pension overseas this is a benefit crystallisation event (BCE) and they use up part of their SFT or PFT. The proposed changes in the Finance Bill will also make the automatic vesting of a PRSA at age 75 a BCE.

Taxation treatment of retirement benefits

Retirement Lump Sum

Lump Sum	**Income Tax**
First €200,000	Exempt
Next €300,000	20% income tax
Balance	Marginal rate income tax, plus PRSI & USC

These limits include all retirement lump sums received since 7 December 2005.

Annuity Income

- Income Tax: An individual in receipt of income from an annuity will pay income tax at their marginal rate.
- PRSI: There is no PRSI liability – Class M.
- Universal Social Charge: Total income is less than €13,000 is exempt from the USC. Where income exceeds €13,000 USC will be due at the rates below depending on the individual's circumstances

Withdrawals from ARFs, AMRFs and vested PRSAs

- Income Tax: Income tax is due on all withdrawals at the individual's marginal rate.
- PRSI: PRSI is due at the following rates depending on the individual's age 4% PRSI is due on all withdrawals before age 66 – Class S. There is no PRSI liability from age 66 – Class M
- Universal Social Charge: Total income is less than €13,000 is exempt from the USC. Where income exceeds €13,000 USC will be due at the rates below depending on the individual's circumstances

Universal Social Charge Rates (2016)

Income Amount	**USC Rate**
Income up to €12,012	1%
Between €12,012 and €18,668	3%
Between €18,668 and €70,044	5.5%
Income in excess of €70,044	8%

Full medical card holders and those over age 70 pay USC at the following reduced rates unless they have earnings greater than €60,000.

Income Amount	USC Rate
Income up to €12,012	1%
Income in excess of €12,012	3%

Standard Fund Threshold

The Standard Fund Threshold (SFT) is the maximum pension an individual is allowed at retirement for tax purposes. This is a lifetime limit and includes all pension benefits taken since 7 December 2005.

The Standard Fund Threshold is currently €2,000,000.

At retirement any amount over the SFT is subject to income tax at the higher rate, currently 40%. This tax is normally deducted from the pension fund. The legislation also allows that this tax could be paid by a payment from the individual or his ARF to the pension administrator which may be of use in some circumstances relating to DB benefits.

Clients cannot use any tax credits or allowances to reduce this liability and the tax deducted cannot be offset against any other tax liability.

The only exception to this is where standard rate income tax was paid on the retirement lump sum, in which case the tax deducted from the retirement lump sum can be used to offset the tax due on any excess over the SFT, see example below.

		Income Tax	PRSI	USC
Fund Value	€2,200,000			
Standard Fund Threshold	€2,000,000			
Gross Retirement Lump Sum	€500,000 (25% of €2m)			
Tax Free Amount	€200,000			
Balance	€300,000	at 20% = €60,000		
Net Retirement Lump Sum	€440,000			
Excess over SFT	€200,000			
Gross Tax on excess over SFT		at 40% = €80,000		
Less tax deducted from Lump Sum		- €60,000		
Net Tax on excess over PFT		€20,000		
Fund value less tax on excess	€2,180,000			
Fund value available after lump sum	€1,680,000			
If invested in an AMRF / ARF		Will apply at client's marginal rate	Will apply up to age 66.	Will apply at client's rate.
If used to purchase an annuity		Will apply at client's marginal rate	n/a	Will apply at client's rate.
If taken as an immediate lump sum		Will apply at client's marginal rate	Will apply up to age 66.	Will apply at client's rate.

APPENDIX 2 – Further information and glossary

What were the drawdown options before Finance Act 2016?

If a client aged 75 or over has an 'unvested' PRSA or 'unvested' Personal Pension (RAC) then there was no requirement to draw any income from the plan.

If the client aged 75 or over had a vested PRSA their options were

- Irish Life automatically pay a distribution of 5% of the value of their vested-PRSA in early December each year.
- No option to withdraw any further amount directly from the vested-PRSA
- Option to transfer to an ARF at any stage
- Option to purchase an annuity at any stage

What is a vested RAC?

Personal Pensions are technically known as Retirement Annuity Contracts (RACs). The Finance Bill introduces new terminology for RACs, called "Vested RAC". A vested RAC is not the same as a vested PRSA, as there is no option to use a vested RAC for income drawdown post-retirement, even before age 75. In summary a vested RAC will work as follows:

- A Personal Pension will become a vested RAC on the clients 75th birthday. This is the only way that a policy can become a vested RAC.
- When a Personal Pension becomes a vested RAC this is a Benefit Crystallisation Event, and the value of the policy will be set against the clients €2m Standard Fund Threshold / Personal Fund Threshold.
- It is NOT proposed that the imputed distribution requirement will apply to vested RACs.
- After 31st March 2017 no access will be permitted to a vested RAC, other than the payment of death benefits.
- On death the vested RAC will have the same treatment as if it was an ARF.

Benefit Crystallisation Event

Since 7 December 2005 every time an individual becomes entitled to receive a pension benefit, e.g. retirement lump sum, annuity, ARF, vested PRSA etc. or they transfer a pension overseas this is a benefit crystallisation event (BCE) and they use up part of their SFT or PFT.

The proposed changes in the Finance Bill will also make the automatic vesting of a PRSA and RAC at age 75 a benefit crystallisation event (BCE).

PRSA AVCs

A PRSA AVC plan becomes a vested PRSA when the member takes their tax free lump sum or other benefits from the related main occupational scheme. In the unusual event that benefits have not commenced from the main scheme, the PRSA AVC will become a vested PRSA from their 75th birthday